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STATE FOR EAP/MTS AND EB/TRA
USDOT FOR SUSAN MCDERMOTT

SENSITIVE

SIPDIS

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SUBJECT: SCENESETTER FOR DOT ACTING ASSISTANT SECRETARY SUSAN
MCDERMOTT

SENSITIVE BUT UNCLASSIFIED

¶1. (SBU) SUMMARY: Welcome to the Philippines! The United States and the Philippines have a deep and abiding relationship resulting from the country's half century as a U.S. territory and commonwealth. Many features of the Philippine government are modeled on that of the U.S., and close ties exist in trade and immigration. The more than four million Filipino-Americans constitute the largest Asian ethnicity in the United States, while some 250,000 U.S. citizens reside in the Philippines. Reflecting this important relationship, the U.S. Embassy in Manila is one of the world's largest.

¶2. (SBU) You are coming at an interesting and challenging time. Increased food prices and the global financial crisis have affected the economy, increasing poverty and straining social infrastructure. However, a consensus remains that the relatively less globally integrated Philippine economy will weather the crisis better than many of its neighbors. The political situation remains stable. The government has responded to the crisis mainly through monetary easing, measured fiscal expansion, more aggressive employment promotion efforts, and targeted assistance to affected sectors. We have not seen severe pressure thus far for the government to respond with new protectionist measures. However, with the approach of national elections in May 2010, it may prove difficult to further open the economy, expand revenues, and boost competitiveness. END SUMMARY.

The Economy in Brief

¶3. (U) The United States is the Philippines' largest trading partner, with over \$18 billion in two-way merchandise trade in 2008. Major U.S. exports include electronics and agricultural products. The U.S. is also one of the largest investors here, with over \$6.6 billion in equity. The Philippine economy grew by 7.3 percent in 2007, the fastest pace of growth in over three decades, but slowed to 4.3 percent in 2008, and will further slow in 2009. However, a resilient service sector (particularly a booming Business Process Outsourcing industry) and strong remittances from overseas workers (expected to again hit \$16 billion in 2009, equivalent to more than 10 percent of Philippine GDP).

¶4. (U) There has been limited progress over the past decade in reducing poverty and addressing the inequitable distribution of incomes. Poverty increased between 2003 and 2006 to engulf over a third of the population. Socioeconomic development in the Philippines is uneven, and poverty is characterized by wide disparities across regions and populations, even during periods of high economic growth, and is especially severe in rural areas. Most of the lagging regions and provinces are in Mindanao, while the frontrunners are on the island of Luzon. While Mindanao features some of the country's more progressive cities and municipalities, human development indices of some of Mindanao's most depressed

provinces approximate the world's poorest countries (such as Ghana, Sudan, and Zimbabwe).

The Political Situation

15. (SBU) Then-Vice-President Gloria Macapagal Arroyo assumed the presidency in 2001 after a "people power" movement swept out her predecessor Joseph Estrada, and then in 2004 she was elected in her own right to a full six-year presidential term. Arroyo is a tenacious leader who has faced a series of challenges to her rule, including unsuccessful impeachment efforts and low-level military coup attempts. National elections will be held in May 2010, and although candidates cannot officially declare until November 30, 2009, the campaign is already under way, with many national figures jockeying for position.

Peace Process on Hold

16. (SBU) Although peace talks with separatist Moro Islamic Liberation Front (MILF) insurgents have remained stalled since fighting broke out in August 2008, government and MILF negotiators are pursuing discussions to create a new framework for resuming peace talks. Earlier this year, President Arroyo publicly stated that 2009 would be a "comeback year for peace" and that she would emphasize to all stakeholders that a robust peace process between the Philippine government and the MILF would encourage stability in the region and enhance economic development.

Main Transportation Issues

17. (SBU) The Philippines is an archipelagic state composed of over 7,000 islands. Its principal cities are seaports; 95 percent of the nation's cargo is transported via sea. Despite the high demand for maritime transport, the Philippines' domestic shipping industry is small and uncompetitive, and is hobbled by restrictive maritime policies and inflexible financial regulations. Since 2003, the "roll-on, roll-off" ("Ro-Ro") network of terminals, feeder roads, and commercial routes has helped improve inter-island transport and reduce costs of domestic transportation. Low levels of spending on transport infrastructure through the years has negatively affected Philippine competitiveness. Based on the World Economic Forum's 2006 competitiveness rankings of basic infrastructure, the Philippines placed 89th out of 102 countries surveyed.

18. (SBU) Civil Aviation Safety: The Philippines was downgraded to "Category 2" by the Federal Aviation Administration (FAA) in December 2007. Since then, the Philippines has passed a civil aviation law and established a financially independent Civil Aviation Authority of the Philippines (CAAP). The FAA developed an Action Plan to rectify the aviation safety rating, and will conduct another audit after the plan is implemented. The International Civil Aviation Organization (ICAO) is working with the CAAP to prepare for the next ICAO audit in October 2009.

19. (SBU) Liberalization of Civil Aviation: Powerful vested interests have, until recently, kept the Philippines from liberalizing air services policies. Only in recent years has pressure from Philippine business coalitions started to force liberalization of civil aviation. Following a ten year period (1997-2006) during which the Philippines averaged only one bilateral agreement per year, the government has signed seventeen bilateral air service agreements and three air transportation agreements with ASEAN countries since 2007, paving the way to a unified ASEAN market by 2015.

Human Rights Issues

110. (SBU) President Arroyo has consistently expressed her commitment to resolving the complex problem of extra-judicial killings and has taken several steps in this direction. While many of these deaths and disappearances are more likely attributable to local disputes than to military or police action, it is clear that the government needs to do more to ensure that these crimes are fully investigated and that responsible parties -- whether or not

they are connected to the military or police -- are brought to justice. The problem is closely related to a judicial system which is inefficient and strained beyond its capacity. Problems such as violence against women, abuse of children, child prostitution, child labor, trafficking in persons, and ineffective enforcement of worker rights are also common.

Development Challenges

¶11. (U) Economic development is a key U.S. objective in the Philippines. Development entails key cross-cutting issues, principally: addressing wide disparities across regions; curbing high population growth; improving agricultural productivity; accelerating implementation of basic education and health reforms; boosting infrastructure; harnessing fiscal resources; strengthening the capacity of local government units; effective law enforcement; improving the investment climate; promoting transparency and accountability; addressing peace and security issues; and strengthening public-private-donor partnerships. President Gloria Macapagal-Arroyo has repeatedly called for unity and strong partnerships as the country grapples with global economic challenges and domestic political concerns with limited resources.

Kenney